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A CERTIFIED PUBLIC ACCOUNTANT'S KEY CONSIDERATIONS IN ESTABLISHING A PERSONAL FINANCIAL PLANNING PRACTICE

by
Darrell A. Flynn
Bachelor of Science, Dickinson State College, 1982

A Independent Study

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of the

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for the degree of

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CHAPTER I

INTRODUCTION

Personal financial planning is the most talked about financial service in the accounting industry today. Individuals from all income and wealth levels are seeking and being sold an increasing array of financial services and products. Financial institutions such as banks, insurance companies and brokerage firms are offering advisory services as a lead-in to their financial product sales efforts. Individuals with diverse credentials and backgrounds--investment advisers, pension planners, chartered life underwriters, certified financial planners, chartered financial counselors, broker-dealers, bankers, attorneys and certified public accountants--are responding to the public demand by offering a wide range of services labeled personal financial planning.

Of these professions, accountants have probably provided personal financial planning for the longest period of time. They have been giving personal financial planning advice on a

piecemeal basis for years, but the packaging of total financial planning as a separate, distinct service has only started to develop in the profession over the past few years.[1]

Traditionally, clients had sought accountants' assistance primarily for the preparation of tax returns and for recommendations on how to legitimately reduce their tax liability. But now that more and more Americans are concerned about their financial security, clients are seeking expanded guidance from their certified public accountant.[2]

> What this comes down to, in practical terms, is that a decision which reduces taxes is analyzed not only for its positive impact on cash but also for any potential negative impact on liquidity, risk and debt structure. The optimal strategy also must be consistent with a client's defined short- and long- range goals.[3]

The challenge to the certified public accountant then, is how to collect, organize, and analyze the data efficiently for all these purposes and then communicate the findings with the pros and cons of the alternatives to the client.[4]

This process is called personal financial planning (PFP). It is the development and implementation of total, coordinated plans for the achievement of one's overall

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[1]Dennis R. Meals, "Guidance for Financial Planners," Journal of Accountancy 159 (May 1985): 83.

[2]David L. Unger, "The Activity Approach to Personal Financial Planning," Journal of Accountancy 159 (April 1985): 94.

[3]Ibid.

[4]Ibid.

financial objectives. The idea is to focus on the individual's objectives as the starting point in financial planning, rather than emphasizing the use of one or more financial instruments to solve only some financial problems.[1]

The increased demand for personal financial planning has created a growing awareness among practitioners that personal financial planning services are not confined to large accounting firms or to large clients. Smaller clients often need these services too, perhaps even more than large ones.

As in any new development of a practice, there are a number of considerations to make. For instance, it is suggested that it is a waste of time to generate new services if you cannot honestly give your firm a B+ with respect to the quality, timeliness, and responsiveness of your existing services.[2] Assuming you do rate a B+ or better, the following are a number of reasons for a firm to get involved in personal financial planning:

1) Clients' expect that you will provide these services (the most important reason). Studies by professional organizations and accounting firms have consistently shown that clients first look to their accountants for advice

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[1]Victor G. Hallman and Jerry S. Rosenbloom, Personal Financial Planning, 3d ed. (New York: McGraw-Hill Book Company, 1983), 3.

[2]Robert L. Bunting, "New Services for Clients - How Other Firms are Doing It," The Practical Accountant 19 (March 1986): 74.

about most of their business and financial concerns. Because of the accountants close business relationship with existing clients, they perceive you as the best qualified professional to help them with most financial problems.[1]

2) The professional development of new accountants. Many young accountants are increasingly disenchanted with a steady diet of tax and audit work, and want to be more involved with clients. A personal financial planning practice gives them an opportunity to apply the skills they learned in college to real situations and to develop new skills.[2]

3) Practice development. "It goes almost without saying that the more practical help you provide to clients, the stronger the client-accountant bond."[3] The personal financial plan can also lead to many other services.

4) Increased billings. Because of the bid process commonly used for audits, they are generally considered a commodity product. Personal financial planning, on the other hand, will be recognized by the client as a specialized, distinct service. In addition, clients are generally more willing to pay fees that are based on the value of the service rather than on the time spent on the project.

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[1]E. J. Burton and W. Blan McBride, "Personal Financial Planning," The Practical Accountant 19 (April 1986): 46.

[2]Ibid.

[3]Ibid.

Therefore, personal financial planning fees can be structured on a project basis rather than on an hourly basis making the fee more commensurate with the value provided to the client.[1]

5) Flexibility in scheduling. Because clients' personal financial planning needs are not based on calendar or fiscal year time-frames like their tax and auditing needs, better utilization of personnel and more uniform scheduling is possible when personal financial planning services are added. You can often deliver personal financial planning services at your own convenience.[2]

6) Practice protection. Many of the larger firms are developing greater personal financial planning capabilities and are going after more of the smaller clients. If you are unable to provide that service to your clients, they will seek that service from another source.[3]

7) Satisfaction and enjoyment. Many accountants find personal financial planning much more satisfying and enjoyable than auditing or tax preparation. Personal financial planning allows the accountant to diversify the type of work done and to use his/her creative energy to solve client problems.[4]

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[1]Ibid.

[2]Ibid.

[3]Ibid.

[4]Ibid.

CHAPTER II

PROVIDING PERSONAL FINANCIAL PLANNING

The key to developing a personal financial planning practice is to decide that you want to do it. Providing personal financial planning is not business as usual. It will require improved timekeeping records and a willingness to bill for those casual conversations you gave away in the past. It is a matter of formalizing your services.[1]

After deciding you want to develop a personal financial planning practice, you and other interested members of your firm should attend personal financial planning seminars. The courses in themselves are helpful, and you will learn what other professionals are doing and what works for them.

> Personal financial planning is an art that requires the skillful application of the planner's training in several technical disciplines that historically are separate and distinct professions. As an art form in its infancy as a separate profession, personal financial planning lacks a widely-followed body of promulgated rules or generally accepted standards. While many professions (the CPA profession in particular)

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[1]Ibid.

> bemoan standards overload, the lack of generally accepted guidelines for the delivery of personal financial planning services is one factor that prevents many planners from practicing personal financial planning profitably. A well-trained and experienced planner may have no need for standard operating procedures, but an individual new to the PFP arena or a firm trying to pyramid its personnel will profit by adopting a well-devised system for delivery of personal financial planning services. A standardized but flexible system promotes efficiency, quality, staff development, and best of all profits.[1]

Most people find themselves in need of financial planning to some degree. Some of the more sophisticated techniques tend to be used by those with higher incomes and larger estate or business interests. This is partly so because many of those with more modest circumstances lack information about financial planning. If they were familiar with the techniques, they would use them more. In fact, less affluent people actually may need such planning more than those with greater wealth because each dollar of income or capital means relatively more to them.[2]

Our economic growth, the tax structure, and changes in our social framework over the years have increased tremendously the need for and complexity of financial planning. One product of our affluent society is the increasing number of people who have large levels of income, assets, and the possibilities of gifts and inheritances

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[1]John R. Clay et al., Guide To Personal Financial Planning (Fort Worth: Practitioners Publishing Company, 1986), 1.

[2]Hallman, 5.

within their estates. Such families find themselves, as never before, with a real need for investment, tax, insurance, and estate planning services. For example, many people today, as a result of their hard work, education, and consequent success, have incomes that place them in high federal, state and often local income tax brackets that make income tax planning highly advantageous. Similarly, a number of them, when both the husband's and the wife's estates are considered, have estates that are large enough to be subject to large federal and state estate taxes. For these and other reasons, they are logical candidates for income tax planning and estate planning.[1]

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[1]Ibid., 5-6.

CHAPTER III

TRAINING AND ETHICAL CONSIDERATIONS

Currently there are no national licensing requirements to become a financial planner if investment advice is not given. However, the certified public accountant who is contemplating offering personal financial planning services must know and comply with all federal legislation. The certified public accountant must also comply with professional standards of the American Institute of Certified Public Accountants (AICPA), Securities and Exchange Commission (SEC) rulings and applicable state security laws covering the rendering of investment advice.[1]

Regulatory Legislation

Certified public accountants who are considering offering personal financial planning services must understand the Investment Advisers Act of 1940, as well as SEC release no. 770.[2]

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[1]Meals, 83.

[2]Ibid.

Section 203 (a) of the Investment Advisers Act requires any person who meets the Act's definition for an investment adviser to register under the Act, unless the person qualifies for any of a number of exceptions from registration specified in the Act.[1]

An investment adviser is defined in Section 202(a)(11) of the Investment Advisers Act of 1940 as

> ...any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities, or who, for compensation and as part of a regular business, issues or promulgates analyses or reports concerning securities...[2]

In SEC release no. 770 the staff of the SEC, which administers the act, explains its applicability to financial planning and interprets the definition of investment adviser. The 1981 Release raises the question of whether a certified public accountant is technically giving "investment advice" during a financial planning engagement, especially when the intention is to recommend only generic investments, not specific ones, and whether that certified public accountant or accounting firm must register under the Act. Some certified

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[1]Personal Financial Planning Committee (1985-1986), Issues Involving Registration Under the Investment Advisers Act of 1940 (New York: American Institute of Certified Public Accountants, Inc., 1986), 5.

[2]Ibid.

public accountants have decided to play it safe and register with the SEC.[1]

Further light has been shed on this subject by the AICPA personal financial planning committee which has published Personal Financial Planning Practice Aid 1 entitled Issues Involving Registration Under the Investment Advisers Act of 1940. This publication is designed to assist certified public accountant's in deciding if they must register under the Act. However, it is a good idea to check with an attorney experienced in SEC rulings to determine the soundest course of action in light of the intended planning services.

AICPA Professional Standards and Guidance

In addition to the complex issues concerning presentation and reporting rules, there are two provisions of the AICPA Code of Professional Ethics that merit attention.

First, Ethics Rule (ET) 201A requires that certified public accountants or their firms undertake only those engagements that they can perform with professional competence. Therefore, before a firm adds this service, it should be kept in mind that certified public accountants who offer these services are expected to be well informed about all areas in which they render advice--taxes, estate planning, personal financial statements, retirement plans,

[1]Meals, 83.

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involves gathering information on consumers' wants and needs. Then the firm must plan and develop a product or service that will satisfy the clients wants and needs. After this, the firm must decide how to price, promote and distribute financial planning services.

Marketing is a total system of business activities designed to plan, price, promote, and distribute a want-satisfying financial planning service to present and potential customers. The overall function of marketing for a financial planning firm should be customer attraction and satisfaction.

Analyzing the Competition

Several questions about the competition must be answered before a certified public accounting firm can start developing a marketing plan for personal financial planning services. What are the other firms in your area doing, and what are the going fees? Who else is offering personal financial planning to your clients or prospective clients? Are certified financial planners operating in the area?

These questions should be answered prior to defining the services to be offered, identifying the target markets and selecting marketing strategies and methods.

In addition, several generalizations can be made about the competition. First, many of the competitors sell a comprehensive personal financial plan which may appear to

clients to be similar to a certified public accountant's plan. Second, the certified public accountant's clients will be considered fair game by these competitors. Third, the plans produced by many of the certified public accountant's competitors may be biased by their commission's earned from products offered in conjunction with the plan.[1]

"But it's a reasonable assumption that the CPA's [certified public accountant's] strongest suit is the profession's reputation for independence, objectivity and integrity. Surveys have shown that the public gives high marks to CPAs for these qualities."[2]

There is an obvious need for objective advice that will help the prospective investor evaluate the pros and cons of purchasing products sold by persons who make their living selling insurance, pension plans, securities, tax shelters and other investment opportunities. The first requirement for objectivity is financial independence. The financial planner should not derive any commissions from the investment decisions of his/her client. Therefore, the certified public accountant will have to give strong consideration to only offering fee based financial planning.[3]

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[1]John R. Clay, "Marketing PFP Services," Journal of Accountancy 159 (May 1985): 82.

[2]Ibid.

[3]Rudolph J. Bergwerk, "Personal Financial Counseling By CPAs--A Neglected Service," Journal of Accountancy 145 (May 1978): 51.

> An objective evaluation of the quality of a particular investment is not enough; what is a good investment for one person may be unsuitable for another. Therefore, the second requirement for objective advice is a thorough analysis of all relevant facts. Financial counseling on a piecemeal basis without adequate background information is usually unsatisfactory.[1]

The third requirement for objectivity is the state of mind of the financial planner, who must try to suppress personal preferences while trying to determine those of the client. This is far from easy. For instance, certified public accountants and other tax consultants must keep in mind that the value of their advice is not necessarily contingent upon the amount of taxes that will be saved. At times it may be preferable to pay more taxes in order to bring about the clients desired results.[2]

"While objective advice is a desirable goal, usefulness is more important than abstract objectivity." A thick financial plan detailing the pros and cons of different strategies of an investment is of no use to a client who wants his question answered with a simple yes or no. Even though most problems do not lend themselves to such a solution, many clients feel let down when their certified public accountants are unable to present findings in a simplified form.[3]

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[1]Ibid.

[2]Ibid.

[3]Ibid.

Defining the Service

Before starting a marketing campaign, it's important to carefully define the product that will be sold. Is the accountant adequately trained and competent enough to offer total financial planning, a plan that includes insurance and investment advice, or will the product be piecemeal planning involving income tax projections, estate planning, or cashflow analysis?

"Unless the product delivered to a client is a comprehensive personal financial plan, it's probably unwise to use the label 'personal financial planning' to describe the services."[1] This is not to say that a certified public accountant can not play an important role in developing the personal financial plan. Rather, the more traditional certified public accounting services may involve the certified public accountant acting as the quarterback of the team, utilizing investment and insurance planning done by others which is included in a comprehensive personal financial plan.

Defining the Market

The market can be defined in many terms such as income, net worth, age, sex, location, education, occupation, and

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[1]Ibid.

endless other criteria. Generally, for purposes of marketing personal financial planning services, income or net worth criteria are utilized most.[1]

Personal financial planning is most beneficial to people who have adequate income or wealth levels. In defining the market, the certified public accountant must determine what net worth or income level is appropriate for the target market. An individual with a gross income of over $75,000 would, generally, benefit from financial planning services, as would many in the $50,000-$75,000 range."Minimum net worth levels are somewhat harder to set because the mix of assets may have as great an impact on the potential benefits of planning as the level of net worth."[2]

It is difficult to set an arbitrary minimum net worth. However, the minimum income and net worth levels selected should be sensitive to cost-benefit considerations.

Other criteria, such as occupation, marital status or level of education, are generally ineffective in further identifying the market. However, age may be an important factor in identifying clients for services that focus on estate or retirement planning.[3]

A fruitful secondary market may be business clients with large staffs. A certified public accountant may be able to

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[1]Ibid., 84.

[2]Ibid.

[3]Ibid.

assist business clients in retaining key personnel by providing personal financial planning as an additional employee benefit.[1]

> An illustration of a market definition is as follows: The primary market for PFP [personal financial planning] services is defined as those individual clients whose gross incomes exceed $50,000 and those clients whose incomes are less than $50,000 but whose net worth, excluding personal residence,exceeds $250,000. Business clients that employ more than 50 people constitute a secondary market; that is, the financial planning services may be offered as a benefit to those client's.[2]

A business plan must also be developed. A business plan is a written document that spells out the philosophy and objectives of the personal financial planning practice and how those objectives will be achieved. The business plan will help to (1) identity the opportunities and shortcomings associated with a personal financial planning practice, (2) recognize a firm's strengths and weaknesses, (3) reconcile conflicting views about the practice and (4) to arrive at a set of agreed-upon objectives and tactics in a systematic and realistic manner. The plan's primary purpose is to improve the probabilities of success of implementing a personal financial planning practice. In addition, the development of the business plan will be good experience for developing business plans for clients. It will also bring about a

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[1]Ibid., 86.

[2]Ibid.

better awareness of the talents and interests of the members of a firm.[1]

While developing your business plan, you need to assess the skills of your current staff. Most clients assume their accountant is capable of acting as a financial advisor, but this is not always the case. It is usually wrong to assume that younger staff members are prepared to provide personal financial planning services simply because their academic training is fresh. In most cases, the younger professionals' only exposure to client financial problems has been in an academic setting, where all data were "given" and no significant assumptions were necessary.[2] Key traits for the staff selected would include excellent communication skills, technical competence, analytic ability, strong organizational skills, supervisory ability, and a positive attitude.[3]

It has been observed that accountants from the same firm may come up with radically different solutions to relatively simple problems. Since this could cause image problems for a firm, uniformity of training should be obtained for firm members.[4]

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[1]Burton, 46-47.

[2]Ibid.

[3]Brian S. Meritt, "How to Write a PFP Success Story," Journal of Accountancy 168 (September 1989): 85.

[4]Burton, 47.

It is essential to become familiar with the skill levels of firm members, and then take steps to give them the opportunity to obtain the necessary skills to implement the personal financial planning services described in the business plan. You may also want to get them further training leading to a professional designation of Certified Financial Planner (CFP) or Accredited Personal Financial Specialist (APFS).

CHAPTER V

SELECTING SPECIFIC MARKETING METHODS

Marketing methods are specific techniques utilized for initiating a financial planning engagement. The methods used should be consistent with the firms marketing strategy, the target market and the service to be offered. Marketing methods selected will also depend on their cost per sale. The three most popular types of sales calls used are personal sales presentations, seminar presentations, and direct mail.[1]

Personal Sales Presentations

A program of personal sales presentations on targeted individuals is likely to have the greatest chances of success. For this to work, the person making the presentation must know the product well and be adept at closing a sale.

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[1]Clay, Marketing PFP Services, 86. This chapter is largely based on Clay's article as I believe he covered the marketing aspects of personal financial planning better than any other source.

Success will also vary with the degree to which the potential clients have been screened in terms of the market definition. A professional-looking brochure can also increase the success rate.[1]

A program of personal sales presentations must be well planned and should provide for a follow-up phone call or letter. "The biggest drawbacks of this marketing method to a firm are the limited amount of professional time (generally partner or manager time) available, the training required and the resulting higher cost per contact. This method is, therefore, best used for marketing high-fee services."[2]

A variation to the above is the personal phone call. A personal phone call is not recommended because the product is hard to sell over the phone and a sales call by phone is generally considered a nuisance with much time being wasted trading phone messages.

Seminar Presentations

Seminar presentations are very similar to personal sales presentations as the same message is being given and they involve lots of personal contact. However, the seminar presentation has the advantage of leveraging the certified public accountant's time. A big disadvantage is that if the

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[1]Ibid.

[2]Ibid., 86-88.

seminar is done poorly, it can be a big bust. Therefore the seminar must be well planned.[1]

Another possible disadvantage of the seminar approach is the development cost of the seminar. A well-conceived, professionally done seminar can involve several thousand dollars in direct cost and a potentially greater cost in professional time. In order to save time and money, firms considering seminars should review existing seminar materials that may be purchased. A good source of materials is the AICPA or your State Society office.[2]

Seminar presentations can be more cost-effective when the development cost is spread over a larger population through multiple presentations to prospective clients. For this reason, smaller firms should probably avoid using seminars as a way to sell financial planning services to clients unless they can handle a large increase in financial planning business. The seminar presentation can be an effective and cost-efficient method to communicate basic financial concepts and sell future financial planning opportunities.[3]

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[1]Ibid., 88.

[2]Ibid.

[3]Ibid.

estimated based on assumed success rates, such as engagements or fees generated.[1]

"To estimate the success rates of various marketing methods, a firm will need to consider the appropriateness of the methods given the defined market and the defined service." In addition, there are qualitative considerations which must be made such as the image the firm wishes to project and the personal sales skills of the staff involved. In order to be successful most firms will generally use a variety of marketing methods. What reaches one client may not reach the next.[2]

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[1]Ibid.

[2]Ibid., 88-90.

CHAPTER VI

STEPS IN THE PLANNING PROCESS

The financial planning process basically involves the translation of personal objectives into financial arrangements to implement those plans. To this end, the following are logical steps in the process:

1) Assemble and organize all financial data and documents;

2) Calculate client's present net worth;

3) Analyze client's present income, expenditures, investments and insurance coverage;

4) Project future needs, income and expenditures;

5) Help client identify his personal and economic objectives and their relative priorities;

6) Identify the financial strategies for achieving these objectives; and

7) Use projections to minimize the client's income tax, select investments, plan for retirement, and keep estate taxes to a minimum.[1]

The client's financial plan should be prepared with an overall strategy in mind and be free of product bias. As a fee based, certified public accountant, you are in a position to provide the kind of bias-free advice that will be most beneficial to the client. This is just one advantage certified public accountants have over many other financial planners who take a piecemeal approach, either because their knowledge is limited to parts of the financial puzzle or who have some sort of product bias. In addition, certified public accountants already have the advantage over their competitor's with a network of satisfied clients, an ability to incorporate tax planning into the plan and all the information which is gathered in client files.[2]

Assemble and Organize all Financial Data and Documents

A formal program for a personal financial planning engagement may be compared to a program for an audit engagement. Both are indispensable, but there is an important difference. For personal financial planning the

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1John R. Connell, LaVerne L. Dotson, and Robert E. Zobel, Touche Guide to Personal Financial Management, (Englewood Cliffs: Prentice-Hall, Inc., 1985), 3-1.

[2]Thomas W. Porter, "Personal Financial Management: A Unique Opportunity For Enhanced Client Service," The Practical Accountant 15 (May 1982): 43.

program is not a mandatory work schedule but a comprehensive checklist of what might be needed. The accountant has to decide which information is relevant and necessary for each particular engagement.[1]

Every audit involves a considerable amount of cost and inconvenience, but when the client is required to get an audit and an unqualified opinion is essential, the client has no choice. Collecting data for personal financial planning can be more difficult, since clients may balk at what they consider unnecessary cost and inconvenience, particularly when they personally have to dig up information, fill in questionnaires and look for papers. To keep the process rolling smoothly, the accountant needs to be prepared to explain why each request for details is appropriate and necessary.[2]

Once a client agrees to have a personal financial plan done you are ready to collect the data from the client. A standard questionnaire which is simple for the client to complete yet informative to you, should be developed for this purpose and should cover:

* Personal and family data;
* Statement of net worth;
* Income sources;
* Expenses by major category;

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[1]Bergwerk, 52.

[2]Ibid.

* Summary of income tax information;

* Summary information on retirement benefits;

* Life insurance;

* Plans for children's education, for retirement, and for major discretionary expenditures in the next 3 to 5 years;

* The relative importance of various investment objectives; and

* Primary financial concerns.[1]

Once the client completes the questionnaire, the certified public accountant can begin the analysis.

Calculate Client's Present Net Worth

"The overall goal of financial planning is to have enough resources to reach your personal goals. The best overall measure of your financial resources is your net worth."[2]

Determining net worth is a process whereby the client calculates his/her total assets and total liabilities and then subtracts the total liabilities from total assets. It is a process which is completed when filling out most standard loan applications. The client's net worth is a fundamental starting point for almost everything in financial planning.

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[1]Porter, 43.

[2]Connell, 3-1.

The client's net worth is a measure of financial condition at a particular point in time. It is the end result of choices made in the past. For example, the client may have chosen to acquire an expensive home, recreational equipment and several automobiles rather than invest the money in stocks or other investments. Or the client may have decided to borrow significantly to finance consumer purchases and vacations, and therefore not have a significant net worth because debts will be almost as great as assets.[1]

It is important to review with the client what has been done in the past so it is understood why present net worth is at its current level. But it is even more important to assist the client to evaluate choices which can be made at present to impact on future net worth. If the client's goals are for net worth to increase, here are some choices which can be made:

* Make investments grow by getting a greater rate of return on investments.

* Increase investments by putting aside more each year from current income.

* Reduce debt.

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[1]Ibid., 3-9.

Analyze Client's Present Income, Expenditures, Investments and Insurance Coverage

The certified public accountant needs to analyze the client's current income, expenditures, investments and insurance coverage to get an overall picture of what the client has available for everyday expenses, investments and types of current insurance coverage. From this picture, the certified public accountant can compare the client's current situation with his objectives to determine what strategies are available to the client to better meet his needs.

This information can usually be gathered on forms specifically designed for this purpose. When listing expenditures, the client should separate those expenses that are considered basic lifestyle expenditures and those that are considered discretionary expenditures.

Basic lifestyle expenditures are those expenses that the client cannot avoid without changing his basic standard of living. Housing, food, clothing, health care and transportation account for the largest portion of basic lifestyle expenditures for many people.[1]

Discretionary expenditures are those expenses over which the client can exercise a good deal of control. It is up to the client whether he dines at home or eats out in style and

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[1]Ibid., 4-3.

drops a bundle. Even though the client has a lot of control over the amounts spent on entertainment, vacations, hobbies, and gifts, the client will presumably be spending some amount on each of them every year. However, some discretionary expenditures are more discretionary and less regular than others. Most client's would not buy a new car or a new boat every year, nor would they subject themselves and their budgets to home improvements with such frequency.[1]

Once the income and expenditure information is gathered the certified public accountant should analyze it and interpret the results by looking at choices the client may have. Here are some ways to analyze it:

1. How much of the client's earned income is left for long-term goals and for investments? In their employment years, people should try to set aside no less than 5- and preferably 10-percent of their employment income and invest it. The amount available for investment can be increased by spending less and/or increasing income.

2. Can the client earn more? Maybe the client can make themselves more valuable in the job market by increasing their skills through continuing education courses, or by using time more effectively, or by focusing on job results rather than the details of the job.

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[1]Ibid., 4-4.

3. Can someone else in the client's family earn more? Perhaps the client's spouse can work part-time. If the spouse is already working, perhaps he or she can expand the scope of the job.

4. Does the client's federal income tax amount to more than 20 percent of their employment income? If so, something should be done to reduce the tax bite.

5. Does the combined percentages of the client's basic lifestyle expenditures and discretionary expenditures come to more than 70 percent? If they do, and the client's earned income is more than $50,000 a year, then it is likely that the client could reduce expenditures without seriously reducing their quality of life; and then he could use the difference for making investments.[1]

By getting the client to analyze their income and expenditure patterns periodically, it helps them to be in control of their finances and highlights the areas in which action ought to be taken.

A similar analysis of the client's current investment holdings and insurance coverage is needed at this time to determine how well they fit with the client's overall objectives and what alternatives may be available.

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[1]Ibid., 4-5,6.

Project Future Needs, Income and Expenditures

The certified public accountant needs to project the client's future needs, income and expenditures for approximately the next five years to determine what effects any changes from the current picture may have on long range planning and on the client's objectives.

Such a projection is useful in a number of ways to include tax planning, choosing investment strategies and determining the likelihood of attaining specific objectives.

For most clients, what is left of their employment income after paying current expenses will be their primary means of accumulating net worth and achieving financial security. Therefore, any increase in their employment income without a similar increase in expenditures, or any reduction in expenditures without a similar reduction in employment income, will provide them with that much more money to invest. This is money that can be utilized to help reach future goals.[1]

Every expenditure dollar the client saves means one more whole dollar available for investment. Every additional dollar of employment earnings produces only seventy cents for investing if the client is in a 30 percent tax bracket.

Once the projection is completed, the accountant can determine what changes the client needs to make in his/her

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[1]Ibid., 4-5.

financial situation to achieve desired long-term objectives. The client may need to increase income, reduce discretionary expenditures, manage taxes more effectively, or a combination of the above. These are choices the client can make to increase the amount available for desired long-term objectives. If the client is unwilling or unable to increase the amount needed to meet long-term objectives then the client will have to revise the amounts set aside next year for long-term goals or revise the goals.

This projection should be continually updated for major changes in expectations so the appropriate action can be taken as needed.

Help Client Identify His Personal and Economic Objectives and Their Relative Priorities

"Since personal financial planning is concerned primarily with helping people meet their objectives, the nature of those objectives and the ways they can be met are of critical importance in the planning process."[1] Often the setting of objectives may be the single most important part of financial planning.

As a general principle, it is desirable to formulate and then state the client's objectives as explicitly as possible. This can have several advantages. First, it forces the

[1]Hallman, 17.

client to think through exactly what his financial objectives are. Second, by doing this the client is less likely to overlook some objectives while concentrating unduly on others. Third, when carefully defining objectives, the client may see solutions that had been over looked before. Finally, the explicit determination of the financial objectives establishes a rational basis for appropriate action to realize those objectives.[1]

While the emphasis on particular objectives will change over a family's life cycle, a classification system of personal financial objectives provides a systematic way for identifying specific objectives and needs as follows:

1. Protection against personal risks, which includes premature death, disability, medical care expenses, and property and liability losses;

2. Capital accumulation which should include an emergency fund, educational needs, if any, retirement needs and a general investment fund;

3. A provision for retirement income;

4. A reduction of the tax burden; and

5. Planning for your heirs.[2]

In addition to this breakdown, the following is an example of some questions that could be asked in a

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[1]Ibid.

[2]This information was taken from a personal financial planning questionnaire which was put together by Flynn & Senger, P.C., for use in gathering client information.

questionnaire to be used to determine the client's personal preferences in making investment decisions, which should be ranked in order of priority:

1. How important is it for you to hedge against big losses by spreading your risks (diversification)?

2. How important is it that you have cash available for emergencies or investment opportunities (liquidity)?

3. If we went into a deep economic depression, how important would it be for you to sell your investments at about the same price you paid for them (safety)?

4. How important is it that you get maximum income from your investments this year and next (current income)?

5. How important is it that your investment dollars keep pace with inflation or do better than inflation (future appreciation)?

6. How important is it that you get all the tax relief that may be available to you (tax advantage)?

7. How important is it for you to use borrowed money in hopes of reaping a higher return on your investment (leverage)?

8. How important is it for you to have investments you do not have to watch or worry about (ease of management)?[1]

As the financial objectives are set, the accountant will be able to find and evaluate what trade-offs there are between the client's short-term and long-term goals, the accountant

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[1]Connell, 10-10.

will also investigate the various alternatives your client has for using his financial resources, and then the accountant should help the client decide which ones are the best for him.[1]

Identify the Financial Strategies for Achieving These Objectives

In this step, the certified public accountant analyzes the client's present position in relation to his objectives and then considers alternative ways of remedying any deficiencies found in the present situation. There almost always are problems to solve in meeting at least some of the objectives. Sometimes a client will actually be overprepared in one area but seriously lacking in others. Thus, balancing the plan is important.[2]

At this stage of the financial planning process, the certified public accountant and his client should consider the various alternatives available to meet the objectives, given the client's financial position, personal situation, and investment constraints. Depending on the circumstances and complexity of the situation, these alternatives may be relatively few or they may be numerous and quite complex.[3]

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[1]Ibid., 9-1.

[2]Hallman, 13.

[3]Ibid.

Given the facts of the client's particular situation, his objectives, an analysis of his present financial position, and consideration of the alternatives, recommendations can be made for a financial plan to meet the client's objectives. Naturally, the specific recommendations made for any plan will differ from professional to professional based on past experience.[1]

Use Projections to Minimize the Client's Income Tax, Select Investments, Plan For Retirement, and Keep Estate Taxes to a Minimum

In developing the financial plan, some projections must be made of future economic events in order to get an adequate picture of what your client can expect from his/her investments and to determine what adjustments need to be made. The projections which most often need to be made are those for inflation, interest rates, return on investments and life expectancy.

It is important that these projections are as accurate as possible. Usually the best sources for these projections are economic indicators which are usually published and updated in popular magazines and journals such as Money Magazine or The Wall Street Journal. Life expectancy statistics can usually be obtained from books on that subject at the local library.

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[1]Ibid.

An example of inflation and how a small change in inflation can affect your client's financial plan will be used here to give an idea of how important it is for projections to be as accurate as possible and why such economic considerations must be made.

How to plan for inflation and perhaps deflation is difficult indeed. Obviously, since one cannot foretell the future, the certified public accountant cannot be sure which will occur, and when, and in what magnitude.

However, it is possible to adjust your client's objectives as to future financial needs for assumed rates of inflation on the basis of the person's perceptions and belief as to what will happen in the future. Let us assume that your client, a Mr. Jones, is age 50 and estimates that he and his wife will need a retirement income after income taxes of about $2000 per month by the time he reaches age 65, or in 15 years. If it is assumed that the price level in the economy (as measured, for example, by the Consumer Price Index) will remain stable over this 15-year period, then Mr. Jones and his wife need only plan to have a retirement income of $2,000 per month at his retirement age of 65. If, however, this assumption is not deemed to be realistic in view of past inflationary trends, and if an inflation rate of, let us say, 6 percent is assumed for the next 15 years, then their retirement income objective, to be realistic, should be adjusted for the expected inflation. Assuming a 6 percent

compounded annual reduction in the value of the dollar, $1 today will be worth only 41.73 cents in 15 years. This is also the present value of $1 due at the end of 15 years at 6 percent compounded interest.[1]

Therefore, to convert a retirement income objective of $2,000 per month in current dollars to a corresponding dollar amount of equal purchasing power starting 15 years from now, assuming a 6 percent per year inflation rate for the 15-year period, divide the $2,000 per month by the present value of $1 due at the end of 15 years at 6 percent compound interest (or 0.4173). The result is a retirement income objective expressed in terms of the assumed price levels that will exist when Mr. Jones reaches age 65 of $4,793. When adjusted for assumed inflation, the Jones's retirement income objective might require somewhat different planning than otherwise would have been the case.

It is important that the certified public accountant consider all of these factors when projecting a client's income taxes, investment performance, retirement needs and potential estate tax liability.

Periodic Review and Revision

No plan, once developed and implemented, should be considered as "engraved in bronze." Circumstances change, and the financial plan must change with the circumstances.

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[1]Ibid., 35.

There are births, marriages, divorces, deaths, job changes, different economic conditions, and a host of other factors too numerous to mention that may make revisions in financial plans desirable or even necessary. Therefore, the final step in the process is adopting a procedure for periodic review and needed revision of the personal financial plan.

CHAPTER VII

CONCLUSION

Personal financial planning represents a service that can be both professionally and economically rewarding. Every certified public accountant who prepares tax returns has clients who need financial planning. By providing this service the certified public accountant will be able to generate more fees, develop a closer relationship with his clients, and possibly be professionally satisfied with the additional challenges such planning will provide.

In order to be successful at financial planning, the certified public accountant must insure that he is competent to perform the services, that a good marketing plan is in place, and that an efficient program is available to develop the plan. Once personal financial planning services are being offered, the certified public accountant will be surprised by the additional services which can be generated as his/her expertise is brought to a broader range of client needs.

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